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GEOGRAPHIC MARKETS IN BANK MERGERS:
A POTPOURRI OF ISSUES

MICHAEL A. GREENSPAN†

I. INTRODUCTION

One of the ways in which a merger can be anticompetitive is if it eliminates substantial existing competition between the merging companies. One step in making that determination is to define the geographic market(s) in which the companies operate. This Article analyzes several aspects of defining these geographic markets. Part II provides a brief overview of the laws, forums and procedures for analyzing the anticompetitive consequence of mergers, both for businesses generally, and for bank mergers in particular. Part III discusses the manner in which the banking agencies and the Department of Justice (DOJ) determine geographic markets. Part IV briefly explores a recent development in antitrust; specifically, the unilateral effects analysis that some claim does away with the need to determine the appropriate geographic market. Finally, Part V notes that Congress allowed a slightly more expansive standard for bank mergers, permitting them to be consummated if the convenience and needs of the community clearly outweigh the anticompetitive effect. Part V then asks if the merging banks can offset positive convenience and needs factors in geographic market A against anticompetitive effects in market B.

II. OVERVIEW OF THE ANTITRUST ANALYSIS OF MERGERS

The United States places great, but not total, reliance on the free market system to allocate resources fairly and wisely (or at least in accordance with the desires of its citizens). Many people believe, however, that left to their own devices markets will tend to

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monopolize (the presence of a single supplier of a product or service). To stop this monopolization, the antitrust laws are intended to prevent anticompetitive acquisitions. In theory, those who believe most vigorously in "free market" solutions and who are most strenuously opposed to government intervention in the market, should be most in favor of strong antitrust laws to insure that free markets exist.

Companies cannot merge\(^1\) if their transaction is proved to violate any of three antitrust laws: Section 1 or section 2 of the Sherman Act\(^2\) or section 7 of the Clayton Act.\(^3\) These laws are equally applicable to bank mergers, although the forums, procedures, and defenses applicable to the mergers are adjusted to take into account that banking is a highly regulated industry.\(^4\)

Section 1 of the Sherman Act states that "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal."\(^5\) Section 2 of that Act prohibits unilateral monopolization and attempted monopolization, as well as monopolization by combination or conspiracy. Specifically, it provides that "[e]very person who shall monopolize, or attempt to monopolize, or combine or conspire with any person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony ..."\(^6\) Finally, section 7 of the Clayton Act prohibits mergers or acquisitions "in any line of commerce or in any activity affecting commerce in any section of the country, [where] the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly."\(^7\)

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1. For simplicity, I define a "merger" as any transaction through which a company acquires control of all or any part of the assets of another.
4. There is a fourth law that is applicable to mergers generally, but which is not applicable to bank mergers. The Federal Trade Commission may challenge a merger or acquisition as a violation of section 5 of the Trade Commission Act which, in relevant part, prohibits "unfair methods of competition." 15 U.S.C. § 45.
When a transaction is between nonbanking companies and it meets various size criteria, the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR Act) requires that the merging parties give information about the transaction to the DOJ and the Federal Trade Commission (FTC). These two federal antitrust agencies decide between themselves which agency will pursue the transaction. Thereafter, that agency may solicit additional information from the merging companies, and should the agency view be negative, it will attempt to work with the parties to fashion an acquisition that the agency believes is not anticompetitive. Failing that, the agency will challenge the transaction in a federal district court as being a violation of one of the three antitrust laws previously mentioned.

Early case law stated that section 7 of the Clayton Act was intended to reach incipient anticompetitive effects not reached by section 1 of the Sherman Act. More recent cases have suggested, however, that judicial interpretations of the two acts have converged. In any event, currently either section 7 is the easier standard to establish or it is the same standard as in section 1. Either way, the DOJ and the FTC almost always attempt to establish the standard of section 7 when challenging mergers.

Banking is among the more regulated industries in this country. Individual banks have "primary federal regulators," and companies that control them are subject to additional regulation by the Board of Governors of the Federal Reserve System (Fed). Those regulators have the responsibility to insure the safety and soundness of institutions under their purview by examining them, by passing rules and regulations, and by reviewing certain transactions in which they propose to engage.

10. See United States v. Rockford Memorial Corp., 898 F.2d 1278, 1282-83 (7th Cir.).
11. The Office of the Comptroller of the Currency (OCC), a part of the Treasury Department, supervises federally chartered banks (called national banks). The Board of Governors of the Federal Reserve System (Fed) is the federal supervisor of state chartered banks that choose to join the Federal Reserve System; the Fed shares supervisory authority with the state Banking Commissioner. The Federal Deposit Insurance Corporation (FDIC) is the primary federal supervisor of state chartered banks with federally insured deposits that do not choose to join the Federal Reserve System; here again, the FDIC shares supervisory responsibilities with the state Banking Commissioner.
Regarding the regulators' role in reviewing proposed transactions, the Bank Merger Act\(^{12}\) requires that a federal bank regulator give its prior approval before any bank with federally insured deposits may merge with another. In addition, the Bank Holding Company Act\(^{13}\) requires the Fed to give its prior approval before a bank holding company may acquire a bank. At the time Congress imposed these requirements, it considered whether a review of the competitive consequences of the merger should be performed by the antitrust agencies (the DOJ or FTC) or the banking agencies (the OCC, Fed or the Federal Deposit Insurance Corporation (FDIC)). It decided that both the antitrust agencies and the banking agencies should perform a review.

In a bank merger or bank holding company acquisition of a bank, the HSR Act does not apply.\(^{14}\) Instead, the applicant files information about the transaction, including its competitive consequences, with the appropriate banking agency.\(^{15}\) The agency gives a copy of the application to the DOJ and requests its views on the competitive consequences of the merger. If, despite the DOJ's negative comments, the agency approves the transaction, the DOJ has thirty days in which to challenge the transaction as being a violation of the antitrust laws. If the DOJ challenges the transaction, the DOJ receives: (1) a \textit{de novo} review of the transaction; and (2) an automatic stay of its consummation. In such a challenge, review of the agency decision uses the same slightly modified standard for bank mergers that the agency itself used.

With some differences that are discussed in Part V, the Bank Holding Company Act and the Bank Merger Act incorporate sections 1 and 2 of the Sherman Act and section 7 of the Clayton Act.\(^{16}\) The

\begin{itemize}
\item \(^{12}\) 12 U.S.C. § 1828(c) (1994).
\item \(^{13}\) 12 U.S.C. § 1842.
\item \(^{14}\) The procedures for review of the transaction by the antitrust agencies are contained in the banking statutes. \textit{See, e.g.,} 15 U.S.C. § 18a (1994). The HSR Act does not apply to the acquisition of a bank. \textit{See id.}
\item \(^{15}\) When a bank is acquiring federally insured deposits, the applicable agency is the primary federal regulator of the resulting bank. \textit{See} 12 U.S.C. § 1828(c)(2). When a bank is acquiring non-insured deposits, the FDIC reviews the transaction, even if the surviving bank is supervised by the OCC or the Fed. \textit{See id.} § 1828(c)(2)(C). When a bank holding company is acquiring a bank, the Fed reviews the transaction. \textit{See} 12 U.S.C. § 1842(a).
\item \(^{16}\) Section 3 of the Bank Holding Company Act provides:
\textit{The Board shall not approve—(A) any acquisition or merger or}
courts have determined that the Fed can deny an application by a bank holding company on competitive grounds only if the transaction violates those laws.\footnote{17} Presumably, this also is true for the Bank Merger Act, which contains the identical statutory standard.

Under section 7 of the Clayton Act, section 1 of the Sherman Act, and the banking statutes covering acquisitions, there is a five step method of analysis that is uniformly employed by the banking agencies, the antitrust agencies and the courts. The five questions are: (1) what is the relevant product market(s) in which to assess the competitive consequences of the merger;\footnote{18} (2) in what geographic market(s) do the merging parties offer the product(s); (3) what is the impact of the merger on competition in the relevant product and geographic markets;\footnote{19} (4) are there any offsetting factors;\footnote{20} and (5)

\begin{quote}
consolidation under this section which would result in a monopoly, or which would be in furtherance of any combination or conspiracy to monopolize or to attempt to monopolize the business of banking in any part of the United States, or (B) any other proposed acquisition or merger or consolidation under this section whose effect in any section of the country may be substantially to lessen competition, or to tend to create a monopoly, or which in any other manner would be in restraint of trade, unless it finds that the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served.
\end{quote}

\footnote{12 U.S.C. § 1842(c) (emphasis added). The italicized language is not in the Clayton Act but is unique to bank mergers. The standard in the Bank Merger Act is identical. See 12 U.S.C. § 1828(c)(5)(B).}

\footnote{17. See County Nat’l Bancorp. v. Board of Governors, 654 F.2d 1253, 1260 (8th Cir. 1981); Mercantile Tex. Corp. v. Board of Governors, 638 F.2d 1255, 1260-63 (5th Cir. 1981).}

\footnote{18. The banking agencies conclude that the relevant product market is the cluster of services known as commercial banking, while the DOJ disaggregates this market into its constituent parts. In First Union Corporation’s application to acquire Signet Banking Corporation, the Fed specifically rejected a protestant’s request that the Board disaggregate the cluster and focus on a small business lending market. See First Union Corp., 83 Fed. Res. Bull. 1012 (1997).}

\footnote{19. The banking agencies assume that a transaction that unduly concentrates the market will have an adverse effect on the market’s performance. The impact of the transaction on the structure of the market is determined by constructing a Herfindahl-Hirschmann Index (HHI) for the market before and after the acquisition. The HHI is calculated by summing the squares of the market shares of the participants in the market. Thus, the acquisition in a 3 firm market of a competitor with a 10% share by one with a 50% share is described as an increase in the HHI by 100 points to 5200 points ((the post-merger HHI: 60 squared + 40 squared) - (the pre-merger HHI: 50 squared + 40 squared + 10 squared)). Calculation of market share is beyond the scope of this Article. For a general understanding of the Supreme Court’s approach to defining market share, see United States v. Philadelphia Nat’l Bank, 374 U.S. 321, 331, 364-65 (1963). The 1992 Merger Guidelines dictate an inquiry that is “fact-intensive,” a methodology that “requires a thorough economic analysis of the
are the solutions that the parties offer to eliminate any anticompetitive effect acceptable?21

While these steps in the antitrust analysis of mergers have stayed constant, the amount of resources devoted to each has varied. In 1963 for example, the Supreme Court placed its major emphasis on the strong presumption that structure determines performance when determining how the merger would affect competition (i.e., it devoted virtually all of its attention to the first three questions). Over time, however, there has been an increasing emphasis on the fourth question, so that present analysis places increasing emphasis on how a market does and is likely to perform after the merger.22

While the attention to be paid to the fourth question has changed over time, the attention paid to the second question has remained constant. In Part III, I summarize how the banking agencies and the DOJ define the relevant geographic market. While all of the agencies agree that the determination of this area is the second step in the analysis, each of them uses slightly different approaches to making its assessment.

III. HOW THE BANKING AND ANTITRUST AGENCIES DEFINE GEOGRAPHIC MARKETS

A. Overview

In United States v. Philadelphia National Bank,23 the Supreme Court determined that section 7 of the Clayton Act applied
to bank mergers.\textsuperscript{24} One way in which a merger could be anticompetitive is by eliminating a substantial amount of actual competition between the merging parties (this is called a "horizontal merger").\textsuperscript{25} A crucial step in that analysis is to define the geographic market(s) in which the merging parties compete. To determine such a geographic market, the Court stated that "[t]he proper question to be asked in this case is not where the parties to the merger do business or even where they compete, but where, within the area of competitive overlap, the effect of the merger on competition will be direct and immediate."\textsuperscript{26}

This language—the area of "direct and immediate" competition—is subject to several different interpretations. The "service area" approach focuses on any overlap in the area(s) within which the banks obtain their business. The "alternatives for customers" approach focuses on any overlap in the area within which the customers of each bank can look for alternative sources of supply. Finally, the "economic market" definition looks for the area within which economic forces are transmitted freely.

These alternative interpretations can lead to differing geographic markets and differing conclusions as to the competitive consequences of a merger. For example, assume that: (1) the Washington, D.C. metropolitan area is made up of the city itself and the suburbs in southern Maryland and northern Virginia; (2) residents of southern Maryland never go to Virginia but substantial numbers of them commute to the central city; and (3) residents of northern

\textsuperscript{24} This was considered to be a surprising result at the time because the language of the statute applied only to asset acquisitions by a corporation that was subject to the jurisdiction of the FTC. See id. Banks are not subject to the jurisdiction of the FTC.

\textsuperscript{25} The Supreme Court has stated that a transaction could violate section 7 even if it did not eliminate substantial actual competition between the parties. One of the two theories would be if the merger would eliminate a competitor who, though not in the market, was presently affecting the competitive conduct of the acquirer. See United States v. Penn-Olin Chem. Co., 378 U.S. 158 (1964). The other theory is if the merger would foreclose the probability that substantial competition might develop between the merging parties in the future. See United States v. Marine Bancorporation, Inc., 418 U.S. 602 (1974); United States v. Connecticut Nat'l Bank, 418 U.S. 656 (1974). While the possibility exists that the government could win a case that does not involve the elimination of actual competition, the requirements for establishing such a case are exceptionally difficult to establish. Accordingly, an applicant invariably wins today if its merger will not eliminate substantial existing competition between the parties.

\textsuperscript{26} Philadelphia Nat'l Bank, 374 U.S. at 357.
Virginia never go to Maryland but substantial numbers of them commute to the central city.

Now consider several merger scenarios. In scenario A, suppose that two banks in northern Virginia want to merge. The service area theory would focus on northern Virginia since that is the area in which both banks do business. The customer alternatives theory would focus on northern Virginia and Washington, D.C., because, in addition to looking in northern Virginia, a substantial number of customers have the choice of banking in Washington, D.C. The economic markets theory would focus on all three areas because all three areas are tied together.27

In scenario B, suppose that a bank in northern Virginia wishes to merge with a bank in Maryland. Under the service area approach, there would be no geographic market in which the two banks compete for business since neither bank does business in the area in which the other competes. Under the economic markets approach, all three areas together would constitute the geographic market since the areas, as explained above, are tied together economically. Under the customer alternatives approach, the market also would be all three areas since customers of the merging banks would have sources for loans in all three areas.

It is interesting that an applicant sometimes argues for a smaller market and sometimes for a larger one. On the one hand, an applicant will prefer a smaller market if that results in the acquirer and the target being in different markets.28 On the other hand, if the acquirer and the target are in the same geographic market, it is generally helpful to the applicant that the market be as large as possible. Having the market as large as possible generally maximizes the number of competitors and minimizes the competitive consequences of the proposed merger.

27. Suppose, for example, that the Maryland bank eliminated service charges on checking accounts. The city bank would have to react because a large number of customers have the choice of banking in Maryland or the city which would cause the Virginia bank to eliminate service charges for the same reason. In other words, economic forces flow freely throughout the three areas, which is the economists' definition of a market.

28. It is very difficult for the government to prevail if the merger does not eliminate substantial actual competition between the parties. See supra note 25.
With this background, I will briefly discuss how the Fed, the OCC, the FDIC, and the DOJ define the relevant geographic market in which to assess the competitive consequences of a bank merger.

B. The Fed’s Approach to Defining Geographic Markets

The Fed clearly falls into the “economic market” camp. The twelve Federal Reserve Banks, which in a sense are regional offices of the Fed, have predefined banking markets over the entire country. In general, these markets remain unchanged regardless of the banks that are merging and the services they offer. For example, in our hypothetical merger discussed above, all of the banks in Washington, D.C., northern Virginia, and southern Maryland are part of the Washington, D.C. banking market regardless of the location of the merging banks within that area.

In defining these markets, the Federal Reserve Banks look for “worker commuting patterns (as indicated by census data) and other indicia of economic integration and transmission of competitive forces among depository institutions.” This data includes shopping data and surveys of bankers, consumers, and owners of small businesses. The Fed will exclude some data of economic integration in order to focus on data showing competition for banking services. Oftentimes the Fed’s markets coincide with those defined in the Rand-McNally Commercial Atlas (these areas around

29. As noted, the Fed defines the relevant product market as the cluster of services known as commercial banking, and they draw the relevant market to fit this product. On rare occasions (generally in response to protests) the Fed considers whether a merger would have a different competitive impact if the product market were different. Obviously the geographic market can change with changes in the product market. The Fed, however, has never decided an application based on these different product markets.


32. In the BancSecurity order, the Fed stated that “BancSecurity maintains that the designation of Tama and Marshall Counties as a Rand-McNally basic trade area and the overlap of school district boundaries between the counties, among other things, support its contention that the relevant banking market should be larger. The Board notes that these delineations are made for purposes not related to the competitive overlap between depository institutions and the facts of this case, including those noted above, indicate that these delineations do not adequately reflect the area in which competition for banking services is real and immediate.” See id.
cities are defined based on economic integration and are known as Rand-McNally Areas (RMAs)).

To summarize, the Fed predefines economic markets based on evidence that shows the area within which economic forces on banks are uniformly transmitted. An applicant can submit evidence justifying a different "economic market," but the Fed rarely changes the definition.33

C. The DOJ's Approach to Defining Geographic Markets

The DOJ and the FTC have promulgated a document that describes the methodology used by both when analyzing the competitive consequences of mergers and acquisitions. The document, known as the 1992 Horizontal Merger Guidelines,34 describes the analysis used for both bank and nonbank mergers. Section 1.2 describes the methodology that the agencies use in defining the relevant geographic market. In essence, the methodology is aimed at finding the geographic area in which a hypothetical monopolist could profitably impose a "small but significant and nontransitory" increase in price (generally five percent in one year). The DOJ (and the FTC) start with the area in which the service areas of the merging parties overlap, if any, and determine whether a monopolist in that area could raise prices with impunity. If it could not, it must be because the monopolist in that small area would face competition from organizations located in a somewhat broader area. By continually expanding the geographic market until it includes all organizations that, in fact, compete in an area, the DOJ ends up with a geographic market that is, or that approximates, the economic market.

However, there is, or may be, one significant difference between the economic markets that the Fed and the DOJ define. The geographic market is intimately related to the product market because it looks for the area where competition for that product will be affected by the merger. As far as the banking agencies are

33. One case in which the Fed changed the market was a case on which the author prepared the application for reconsideration. See Hawkeye Bancorporation, 64 Fed. Res. Bull. 974 (1978).
concerned, the relevant product market for a bank merger is the cluster of services known as commercial banking. The DOJ, on the other hand, has disaggregated the cluster into several constituent parts. The DOJ starts by considering a separate product market for retail banking services and commercial banking services. However, the DOJ will refine its product market to take account of the actual product that the merging banks and the others in the local area offer.

To date, the DOJ has never concerned itself with the impact of a transaction on the retail product market.\(^{35}\) It has, however, looked closely at a market for loans to middle market companies; and has looked at a market for small business loans, for unsecured small business loans, and for those companies that offer the cluster of services required by small businesses. Note that the only time the DOJ has litigated its disaggregated market definition, the distinct court rejected that definition in favor of a definition based on the cluster of services offered by commercial banks.\(^ {36}\)

The DOJ’s disaggregation of the relevant product market can have a direct impact on the relevant geographic market. The purpose of geographic market definition is to define the potential customers of the merging parties that could be affected by the merger. The DOJ has concluded that small businesses are locally limited in their credit sources. Accordingly, when the DOJ focuses on some aspect of the small business market, it sometimes finds the relevant geographic market to be much smaller than the Fed’s market, which is based on the cluster of commercial banking services as the relevant product market.

This often has a remarkable impact on the result of the analysis. When two banks are located in the same geographic market, and that market is made smaller, the effect of the merger generally is to reduce the number of competitors and increase the effect of the merger on competition. A good example is the 1992

\(^{35}\) As noted, the Fed does not disaggregate the cluster into its constituent parts. Steve Rhoades, the chief of the Fed’s banking markets section, however, has said that if the Fed were to disaggregate, he would urge it to focus on the competitive consequences of the merger in the retail banking market. Despite the presence of countless credit card offers and of electronic banking, he believes that there is a correlation in the retail market between a small number of local banks and high prices.

merger of Society Corporation with Ameritrust Corporation. The Fed approved the application after examining its impact on ten Ohio markets, including the Cleveland market. While the Fed required significant divestitures in several markets, it found that none were required in the Cleveland market, which the Fed defined to include all or parts of eight counties in the Cleveland metropolitan area.\textsuperscript{37} The DOJ focused on the small business loan market, finding that these borrowers were limited in the places from which they could obtain these loans. Accordingly, the DOJ did not have a "Cleveland market," and defined geographic markets on a county-by-county basis. The DOJ found significant anticompetitive effects in two of the Fed’s eight counties, and required divestitures in those markets.\textsuperscript{38}

The banking industry has been unwilling to challenge the DOJ when it finds anticompetitive effects based on the disaggregated product market and the smaller geographic market that such a product market sometimes implies. The simple fact is that in all of the transactions to date, the divestiture of a few additional offices constituting a small percentage of the assets being acquired has been sufficient to assuage the DOJ.

As a general matter, however, the industry continues to believe that the mergers to which the DOJ objects should be permitted. The industry’s two main theories are that there are many nonbank alternatives for banking services and that small businesses are not as locally limited as the DOJ asserts. In that regard, recent evidence collected by the Fed’s staff both supports and undercuts the industry’s contention that small businesses are not locally limited.\textsuperscript{39} On the one hand, the evidence shows that a substantial number of out-of-market lenders are making loans to local businesses. On the other hand, that evidence also shows that, on average at the present time, the percent of each organization’s borrowing from out-of-market lenders is only a small percentage of its total borrowing.

D. The OCC's Approach to Defining Geographic Markets

The OCC has concluded that, as a general matter, mergers are efficiency-enhancing methods of increasing benefits to consumers. Accordingly, the OCC will approve virtually all mergers that the DOJ clears. Two commonly cited examples of the OCC's liberality are its willingness to use any geographic markets definition that permits the merger, and its use of a *de minimis* theory to approve certain mergers that appear on the surface to be anticompetitive.

There is no published support for the first proposition. There is substantial evidence that the OCC considers the service areas of the merging banks as well as the Fed's "economic market". However, the OCC staff has confirmed that there is no case in which the OCC has had to rely on the service area definition to the exclusion of the Fed definition. In all cases in which there have been substantial anticompetitive effects in the Fed-defined market, the OCC has found some alternative method of justifying its approval. Nevertheless, the view persists among experienced practitioners that the OCC would use the service area approach to define the relevant market if that were the only method for that agency to approve the transaction.

There is, however, substantial evidence for the OCC's *de minimis* theory. The seminal case is the 1983 merger of National Bank of Oxford into the National Bank and Trust Company of Norwich. In that case, the OCC approved the merger on the theory that the relevant geographic market was too small to be a "section of the country." There is no exact statement of the rule. It certainly applies when the population of the county is approximately 10,000 or less. It also may apply when the population of the county exceeds that number but the population of the town in which the target bank is located is small.

40. In *Application of Zions First Nat'l Bank, Salt Lake City, Utah*, Corp. Decis. #97-82 (Sept. 1997), the OCC stated that "[i]n defining the geographic markets, the OCC considered the Federal Reserve bank of San Francisco's market delineations, as well as evidence of the areas from which the involved banks derive the bulk of their deposits." *Id.* at n.2.

41. Telephone interview with Mitchell Mertins, OCC staff, in Washington, D.C.
It is unclear whether the OCC’s conclusion is based on its interpretation of the Bank Merger Act, or whether it is based on the assumption that the DOJ is unlikely to “waste” resources challenging a merger so small. Regardless, it appears that the OCC will approve such mergers, while the other agencies will not.

E. The FDIC’s Approach to Defining Geographic Markets

The FDIC’s views on the competitive analysis of merger transactions are contained in a 1989 policy statement. While the FDIC recently has proposed to update that statement, its position on geographic market determination is the same in both statements: The relevant geographic market(s) includes the areas in which the offices to be acquired are located and the areas from which those offices derive the predominant portion of their loans, deposits, or other business. The relevant geographic market also includes the areas where existing and potential customers impacted by the proposed merger may practically turn for alternative sources of banking services. In delineating the relevant geographic market, the FDIC will also consider the location of the acquiring institution’s offices in relation to the offices to be acquired.

The FDIC’s Policy Statement suggests an approach that is part “service area” based and part “customer alternatives” based. In actuality, the FDIC seems to be responsive to applicants’ arguments as to the relevant market, sometimes accepting the Fed’s “economics

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42. The OCC cited cases such as *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962), and *Pargas, Inc. v. Empire Gas*, 423 F. Supp. 199 (D. Md. 1975), aff’d, 546 F.2d 25 (4th Cir. 1976). In *Brown Shoe*, the Supreme Court considered the legislative history of the Clayton Act and concluded that it was intended to apply in “economically significant” areas. In *Pargas*, the Court held that markets in that case with more than 10,000 people were economically significant. These cases suggest that there is a market that would be too small to be recognized as a relevant geographic market. However, there is no case in which a court has supported the theory, and in *United States v. County Nat'l Bank of Bennington*, 339 F. Supp. 85 (D. Vt. 1972), the district court rejected the OCC’s claim that a market of 24,000 people was too small to be cognizable as a market. See *United States v. American Bldg. Maintenance Indus.*, 422 U.S. 271 (1975) (distinguishing *County Nat’l Bank*).


45. Id. at 52,879.
markets" definition as well. There are two major points about the FDIC’s approach. First, unlike the Fed, the FDIC determines the market in relation to the banks that are merging (while the Fed predefines markets for all mergers). Second, since the FDIC has not invested significant resources in market definition (or pre-definition), the FDIC is more willing than the Fed to modify its market definition in response to information that the applicant submits.

IV. UNILATERAL EFFECTS ANALYSIS

Previously I stated that there is a five step analysis used by the antitrust and banking agencies. The five questions are: (1) what is the relevant product market(s) in which to assess the competitive consequences of the merger; (2) in what geographic market(s) do the merging parties offer this product(s); (3) what is the impact of the merger on competition in the relevant product and geographic markets; (4) are there any offsetting factors; and (5) are the solutions that the parties offer to eliminate any anticompetitive effect acceptable?

This is certainly true as far as the banking agencies are concerned. These agencies note that the economic research that correlates concentration with higher prices, and in step three, they go directly from the fact that a merger will increase concentration to a presumption that the market will operate in an anticompetitive manner. The DOJ, however, is a litigating agency, and has concluded that it cannot simply take “administrative notice” of the correlation between concentration and prices, but must have a theory why the correlation occurs. In the Merger Guidelines, it offered two explanations: (1) increases in concentration could increase the possibility of collusion between the smaller number of remaining competitors, and (2) concentration might have an impact on performance even in the absence of collusion. This second “explanation” of why a merger that increases concentration is illegal has come to be known as “unilateral effects” analysis.

In the early years of the Guidelines, unilateral effects did not receive much attention. In the last two or three years, however, the search for these effects has come to dominate discussions with the antitrust agencies. This is important to this Article because under
one such form of unilateral effects analysis it is claimed that it is not necessary to define the relevant geographic market. The DOJ is not currently using unilateral effects analysis in analyzing bank mergers. However, I am including a brief description of the theory for two reasons. First, it is very much on the cutting edge of antitrust. Second, since it is evolving so rapidly, there is at least a possibility that the DOJ could use it in analyzing bank mergers in the future.

There were six articles on unilateral effects analysis in the Spring 1997 issue of Antitrust Magazine. These articles explain that under this analysis, the antitrust agencies try to directly predict what will happen to the prices of products sold by the merging companies rather than, or as well as, determining the relevant product and geographic market, and market shares, etc. In one version of unilateral effects analysis that may or may not be limited to sellers of “differentiated” products, the agencies try to calculate the impact of a merger on prices by calculating the elasticity of supply and demand functions for the merging companies. In the case of products sold in supermarkets, these functions can be calculated (or approximated) by analysis of scanner data.

The approach undertaken by this kind of analysis is to find if there is a class of customer who will choose only between a product sold by each of the merging firms. After the merger, that class of customer will be at the mercy of the survivor, since the customer will have no other alternative. In what seems to be magic to the nonmathematically inclined layman, economists claim to be able to calculate (given enough of the right kind of data) how many people would be negatively impacted in this way by the merger and how much the price could rise with respect to them.

Of course there are economists and lawyers who find this information less than persuasive. Among other problems, it may be that one chooses between Cornflakes and Raisin Bran each morning. But it is also true that if those companies merge and try to raise the price of Raisin Bran significantly, one may be more than willing to try some entirely different cereal.

Thus far, the unilateral effects analysis has played no role in analyzing the anticompetitive effects of bank mergers. Were it to become the dominant view, however, its proponents claim that it
would do away with the determination of markets and market shares that have formed the backbone of antitrust analysis to date.

V. CAN POSITIVE EFFECTS IN ONE MARKET OFFSET ANTICOMPETITIVE EFFECTS IN ANOTHER?

Although an acquisition violates the antitrust laws, courts will permit the acquisition of a commercial organization if the target is a "failing company" and if there are no less anticompetitive solutions to the failing company's problems.\(^{46}\) This idea was incorporated into the banking statutes in an expanded form. The Bank Holding Company Act and the Bank Merger Act provide that any proposed merger transaction which substantially lessens competition shall not be approved by the responsible banking agency unless it finds that the anticompetitive effects are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served. This has come to be known as the "convenience and needs" defense.

The legislative history of the "convenience and needs" defense makes clear that Congress intended it to be an expansion of the "failing company doctrine," available where the target is merely stagnant or floundering, rather than actually failing.\(^{47}\) Because it is based on the failing company defense, however, when a banking agency has approved a transaction on convenience and needs grounds, it generally has stated that there were no less anticompetitive solutions to the bank's problems.\(^{48}\) There may be at least one case, however, in which the Fed approved a transaction that it viewed as anticompetitive and the order approving the merger does not indicate the absence of alternative solutions.\(^{49}\)

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49. See First of America Bank Corp., 70 Fed. Res. Bull. 516 (1984). The Order states that the Board is approving the application because "significant benefits to the convenience and needs of the community that would result from this transaction outweigh the anticompetitive effects of [the] proposal," and "[t]he Board has determined that
There is an interesting aspect of the "convenience and needs" defense that is relevant to the present article. The Supreme Court has held that:

It is settled that courts should give weight to any reasonable construction of a regulatory statute adopted by the agency charged with enforcement of that statute. [A banking agency] is charged with the enforcement of banking laws to an extent that warrants the invocation of this principle with respect to [its] deliberate conclusions as to the meaning of these laws.  

This is especially true in the recent past when the Supreme Court has given great deference to the reasonable constructions by the OCC of statutes within the scope of its authority.

Assume that: (1) Bank A and Bank B are national banks that compete in geographic markets 1-10; (2) the merger of these banks would violate the antitrust laws in market 1; (3) there are positive "convenience and needs" factors in markets 2-10; and (4) the only way to achieve those benefits is through the merger of Banks A and B. Assume further that: (5) the OCC approves the merger arguing that the "convenience and needs" considerations in markets 2-10 clearly outweigh the violation of the antitrust laws in market 1; and (6) the DOJ files suit to block the transaction. The question is whether a court should give deference to the OCC's determination and support if it is at all reasonable.

There are two preliminary matters to be addressed. First, the Supreme Court has given deference to an agency that has sole

consummation of the proposal is consistent with the public interest ... and should be approved." Id. at 517. However the statutory scheme permits the Board to deny on competitive grounds only if the transaction violates the antitrust laws and it permits the Board to approve of a transaction that violates the antitrust laws only if the Board finds that the anticompetitive effect is "clearly outweighed." Perhaps the best way to understand the case is to assume, despite the anticompetitive language, that the Board never decided that the anticompetitive effect was enough to violate the antitrust laws. If so, there is no need for the convenience and needs effects to "clearly outweigh" the anticompetitive effect.


responsibility for interpreting a statute. The OCC, however, shares interpretation of the Bank Merger Act with the two other banking agencies — the FDIC and the Fed. Each has exclusive authority with regard to institutions under their control. While I can point to no precedent, I see no inherent problem with courts upholding a view of the OCC as to national bank mergers that is directly contrary to the view of the Fed as to state member bank mergers, as long as both agencies have a reasonable amount of support for their position. To decide otherwise would be to deny one of the banking agencies the deference to which its reasoned conclusion is entitled.

Second, the OCC shares enforcement of the statute, not only with other banking agencies, but with the DOJ as well. Since the issue would arise only if the DOJ was challenging a merger in court, it might be argued that the OCC’s promerger interpretation would be offset by the DOJ’s antimergen interpretation. However, deference is due to agencies that regulate industries. The OCC is entitled to that deference. The DOJ is a litigating agency. As such, its construction should be entitled to no deference. While, again, I can point to no precedent, I believe that the courts should give weight to the OCC’s interpretation if it is reasonable.

Thus, it is at least relatively clear that courts should defer to a reasonable interpretation by the OCC that preceded the court case. It is less clear, however, that the OCC has the discretion to interpret a statute in a manner contrary to the way the courts have already interpreted it. The Supreme Court previously considered the statute and, at least in one context, has decided that a reviewing agency may not offset a positive convenience and needs effect in one market against an anticompetitive effect in another. Accordingly, an extended discussion of that case is necessary to understand its limits.

In United States v. Phillipsburg National Bank, the OCC had approved the merger of Phillipsburg National Bank and Trust Co. and the Second National Bank of Phillipsburg. Both banks were located in Phillipsburg, New Jersey. The OCC based its approval on the lack of anticompetitive effect in the four counties surrounding the towns of Phillipsburg and Easton. The district court accepted the

OCC's geographic market definition which involved an area with 216,000 people and eighteen banks. However, the Supreme Court overturned it in favor of the two towns themselves which had a total population of 90,000.

The Supreme Court criticized the district court's application of the convenience and needs standard. The Supreme Court stated that the district court had assessed "the competitive effect of the proposed merger in the broad, multi-community area that it adopted as the relevant geographic market, while assessing the merger's contribution to community convenience and needs in Phillipsburg alone." The Court added that the geographic market is the area in which convenience and needs must be evaluated:

- Under the approach taken by the District Court, anticompetitive effects in some parts of a relevant geographic market could be justified by community benefits in other parts of it. Such a result would subvert the clear congressional purpose in the Bank Merger Act that convenience and needs not be assessed in only a part of the community to be served, and such a result would unfairly deny the benefits of the merger to some of those who sustain its direct and immediate effects.

Thus, the Court held that it is improper to offset convenience and needs benefits in the four county area against anticompetitive effects in the much smaller Phillipsburg-Easton market contained within it. Would this precedent prevent the OCC or the other banking agencies from approving a merger in all circumstances in which the offsetting benefits partly come from other geographic markets?

There are two arguments that the OCC might advance. First, it has been nearly thirty years since the Phillipsburg case. Banking has changed substantially (particularly with respect to the crumbling of geographic barriers), and Congress has established banking agencies to monitor those changes. It is their job to keep the industry

54. Id. at 370.
55. Id. at 371-72.
modern providing there is enough ambiguity in the statute to permit flexibility of interpretation.\textsuperscript{56}

Thus, in \textit{Smiley v. Citibank},\textsuperscript{57} the Supreme Court affirmed the responsibility and authority of the agencies to change their interpretations of statutes they administer as developments in the industry occur. The Court stated:

Finally, petitioner argues that the regulation is not entitled to deference because it is inconsistent with positions taken by the Comptroller in the past. Of course the mere fact that an agency interpretation contradicts a prior agency position is not fatal.

Sudden and unexplained change [citations omitted], or change that does not take into account legitimate reliance on prior interpretations [citations omitted], may be "arbitrary, capricious [or] an abuse of discretion". 5 U.S.C. § 706(2)(A). But if these pitfalls are avoided, change is not invalidating since the whole point of \textit{Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.}, 467 U.S. 837 (1984) is to leave the discretion provided by the ambiguities of a statute with an implementing agency.\textsuperscript{58}

The second argument (obviously dependent on the facts of the case) is that the decline of geographic barriers now permits mergers whose anticompetitive effect is minimal compared to the large number of people that would be benefited by consummation. This is a difference, the argument would go, in kind rather than in degree.

Consider that in the \textit{Phillipsburg} case the Supreme Court refused to allow benefits to 90,000 people to outweigh disadvantages to 125,000 others. Contrast this with a transaction such as the acquisition by Fleet Financial Group, Inc. of the assets of the failed Bank of New England from the FDIC. Fleet was the winning bidder over Bank of America. The DOJ objected to the transaction on the

\textsuperscript{56} Language that convenience and needs factors must do their offsetting in the community that the merging bank serves, certainly is subject to multiple interpretations.

\textsuperscript{57} 116 S. Ct. 1730 (1996).

\textsuperscript{58} \textit{Id.} 517 U.S. at 1734 (emphasis added).
grounds of its anticompetitive effects in the Bangor, Pittsfield, and Presque Isle-Caribou markets in Maine.

The Fed approved this transaction on the grounds that there were no anticompetitive effects in the three markets claimed. Suppose, however, that the Fed agreed that the transaction was anticompetitive in those three markets, but the benefits to the millions of customers the Bank of New England served in Massachusetts, Connecticut, and Maine far outweighed the limited harm to the few residents in the Maine markets. The convenience and needs defense was adopted when geographic limits on banks were the norm and transactions simply were incapable of benefiting as many people as they are today when geographic limits have been eliminated on all holding company acquisitions.

If faced with this kind of problem, I would advise a banking agency to follow its conscience and its view of where the public interest lay. If the matter was litigated, the agency might lose. I prefer, however, arguing on the side of the angels.

VI. CONCLUSION

There are many issues involved in geographic market determination. However, I have attempted to provide a useful introduction to the field by discussing several of the significant issues in this Article. First, I provided an overview of the competitive analysis of bank mergers. Second, I showed the importance of geographic market determination in considering whether a merger is likely to eliminate a substantial amount of actual competition between the merging parties. Third, I discussed how the banking agencies and the DOJ make this determination. Fourth, I briefly discussed a "unilateral effects" analysis that could do away with the need for geographic market determination in some circumstances. Finally, I argued that a banking agency should be


60. The "fix-it-first" approach taken by the Fed and the DOJ means that these kinds of issues are never litigated. In the actual Fleet case, for example, Fleet agreed to divest a small number of offices in the three markets, which constituted a small percent of the assets it was acquiring. Whether this kind of approach, which tends to assure that the DOJ's positions never get litigated, is in the interest of the public or the banking industry, is beyond the scope of this Article.
able to offset convenience and needs considerations in one market against anticompetitive effects in another.